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Tax Information on Self-Employed Retirement Plans

Note: As this publication went to print, the Internal Revenue Service was considering a change in the return filing requirements for individuals who use Form 5500-C or Form 5500-K. The new system will be effective for plan years beginning after 1979.

Department of the Treasury
Internal Revenue Service

Introduction

This publication discusses retirement plans for self-employed persons and certain partners in partnerships. These retirement plans are sometimes called Keogh plans or HR-10 plans.

If you set up a retirement plan that meets certain legal requirements, you may be able to deduct your contributions to the plan. In addition, the plan and its income will be exempt from tax.

Because of the difficulty of the subjects discussed here, certain technical terms must be used. These are defined in the beginning of the publication to help you become familiar with them.

There are footnotes throughout the publication. These are citations to legal authority. They are included if you would like to refer to the authority for more information.

Some of the discussions are based on Income Tax Regulations that have been proposed but are not yet final. Your Internal Revenue office should be able to tell you if there have been any changes since this publication was printed.

Definitions

To help explain the rules for qualifying a retirement plan for tax exemption, you should first understand some of the terms that are used. The following definitions explain the meanings of certain terms used in this publication.

An employee is any person who works for another person or a business firm for pay. Employees are also called common-law employees.

It is possible to be an employee and be self-employed at the same time. A good example is a lawyer who is an employee of a corporation during regular working hours. The lawyer also has an office and practices law in the evening as a self-employed person.[1]

Full-time life insurance salespersons are employees for retirement plan purposes even though they are considered self-employed under common law.[2]

Self-employed person. A person who has earned income from operating an unincorporated business (a sole proprietorship) or who performs personal services as a partner for a partnership is considered a self-employed person, even if there are no profits in a particular year.[3]

If a self-employed person has more than one business and sets up a retirement plan for one business and not the others, each business is considered a separate employer. Only the earned income from the business that sets up the plan is considered for that plan.[4]

Ministers and members of religious orders who are employees are not self-employed even though their income is considered earnings from self-employment for social security purposes.[5]

Example. A minister employed by a congregation for a salary is an employee even though the salary is treated as self-employment income for social security tax purposes. However, fees for performing marriages, baptisms, or other personal services are earnings from self-employment.

Doctors and Christian Science practitioners are considered self-employed if they are not employees.[6]

An owner-employee is a sole proprietor. In a partnership, a partner who owns either more than a 10% interest in the profits or more than a 10% interest in the capital of a partnership is also an owner-employee. A partner who owns a 10% or less interest in the partnership is self-employed but is not an owner-employee.

The profit interest of each partner is generally written in the partnership agreement. If there is no agreement, the interests are determined in the same way as distributive shares of partnership taxable income. A guaranteed payment made without regard to the partnership income is not considered a distributive share of partnership income.

The capital interest of a partner is based on the interest in the partnership assets that would be distributed to that partner when leaving the partnership or when the partnership is dissolved, whichever is greater.[7]

Net earnings from self-employment means the gross income a self-employed person receives from a business minus all allowable deductions for that business. The deductions include contributions made under a plan for employees.[8]

Contributions by or on behalf of an owner-employee may be made to a plan only if personal services are performed by the owner-employee. Owner-employees whose income is only from investments cannot participate in the plan.

Example. Your distributive share of income from an investment club partnership that only invests in, or collects interest on, savings certificates is not net earnings from self-employment.[9]

Limited partners. Net earnings from self-employment do not include the distributions of income or loss of limited partners. However, guaranteed payments paid to limited partners are net earnings from self-employment if paid for services rendered to or for a partnership.[10]

Earned income is income from services. Earned income is also net earnings from self-employment but only for a business in which the taxpayer's services are a material factor in producing income.[11]

You may have earned income from property if your personal efforts helped create the property. For example, authors and inventors create the books and inventions that pay royalties. This earned income includes gains but not capital gains. It includes net earnings from

the sale or other disposition of the property and the transfer of any interest in the property. It also includes licensing the use of property other than goodwill.[12]

Interest income is from the investment of capital and is not earned income.

Income earned abroad that you exclude from income is not earned income for retirement plan purposes.[13]

A business is carried on for livelihood or for profit. A profit motive must be present and some type of economic activity must be involved.

Service as a public official is not a business. Service as a newspaper carrier under age 18 is not a business, but service as a dealer is a business. Service as a sharecropper under an owner and tenant arrangement is a business.[14]

Rules for Plan Qualification

A plan that includes self-employed persons but no owner-employees generally must meet the qualification requirements that apply to plans of corporate employers. Some of these requirements are:

1) The plan must be in writing and must be in effect in the tax year qualification is sought.
2) The plan must be a pension, profit-sharing, annuity, or bond purchase plan that is set up by the employer for the benefit of employees or their beneficiaries.
3) The plan must be a funded plan such as a trust, custodial account, insured, or bond purchase plan.
4) The plan must benefit a certain percentage of employees or a class of employees selected by the employer. In no case may the plan discriminate in favor of highly paid employees through contributions or benefits.

The two types of retirement plans are defined contribution plans and defined benefit plans.[15] A defined contribution plan may be a pension plan or a money-purchase pension plan. However, a defined benefit plan may only be a pension plan.

A defined contribution plan provides an individual account for each person in the plan. Benefits are based on the amount contributed to each account and any income, expenses, gains and losses, and any forfeitures of other accounts that may be allocated to the account.[16]

Forfeitures of accounts may not be allocated to self-employed persons or to owner-employees.[17]

If contributions are geared to the employer's profits, the plan is a profit-sharing plan. If contributions are not based on the employer's profits, the plan is a money-purchase pension plan.

A defined benefit plan sets the retirement benefits. Contributions to the plan must be enough to produce those benefits.[18] A defined benefit plan is a pension plan and can be in the form of an annuity, or bond purchase plan.

Plans are for the benefit of employees or their beneficiaries. A sole proprietor is considered to be both an employee and employer. A partnership is considered to be the employer of each of the partners. A plan that includes self-employed persons must provide benefits for employees without discrimination.

Discrimination in contributions or benefits. A plan may not discriminate in favor of self-employed persons. The total employer contribution on behalf of a self-employed person is taken into account to find if there is discrimination, even if only part of that contribution is allowed as a deduction.[19]

Integration (combining) with social security. A plan is not considered discriminatory because of differences in benefits that favor highly paid employees, if it is properly integrated with social security benefits. The differences in the plan benefits are considered to be offset by social security benefits from employer contributions to the social security system.[20]

To integrate a plan with social security, the maximum amount treated as wages is the same as the maximum amount treated as self-employment income for social security purposes. These amounts follow:[21]

Year(s)	*Amount*
1967-1971	$ 7,800
1972	9,000
1973	10,800
1974	13,200
1975	14,100
1976	15,300
1977	16,500
1978	17,700
1979	22,900
1980	25,900

Plans also may qualify when coverage is limited to a particular class of employees, if that limit does not result in prohibited discrimination. However, self-employed persons cannot participate in a plan for salaried or clerical employees.[22] It should be noted that a defined benefit Keogh plan cannot be integrated.[23]

Base for computing contributions or benefits. A plan may allocate contributions, or determine benefits in proportion to the total compensation of the employees covered, or in proportion to their basic or regular rate of compensation. A self-employed person's total compensation is earned income. A self-employed person's basic or regular rate of compensation is the percentage of earned income that is found by dividing the combined basic or regular rate of compensation of all employees under the plan by the employees' total compensation.[24]

If an employer establishes two or more plans that qualify separately and only one plan covers a self-employed person, the basic or regular rate of compensation of that person is determined by the compensation of the employees who participate in the same plan.

If two or more plans must be considered together, the basic or regular rate of compensation of a self-employed person is determined by the compensation of the employees covered by the plans that are required to be considered together to qualify.[25]

When an excess contribution is made by or for a self-employed person because earned income was figured incorrectly, the plan will not be discriminatory if a proper adjustment is made to remove that excess contribution. Any excess employer contribution may be considered the self-employed person's voluntary contribution unless that person already made the full voluntary contribution.[26]

A plan that includes self-employed persons does not qualify if an employee's compensation is reduced at or about the time the plan is adopted.[27]

A profit-sharing plan that has a fixed annuity fund and a variable annuity fund and covers both employees and self-employed persons may not discriminate in favor of the self-employed persons in its contributions. However, the plan is discriminatory if it allows only self-employed persons to set the percentage of employer contributions that goes into the plan's variable annuity fund. The plan is discriminatory because the self-employed persons can choose the fund that is likely to produce a higher return. The employees have no such right.[28]

A pension plan that allows self-employed persons to choose not to participate in a particular year or to vary the contributions made on their behalf yearly does not qualify.[29]

A defined benefit plan that provides full and immediate vesting of benefit rights is not discriminatory if the "accrued benefit" for any employee is limited to the "maximum basic benefit". For example, a plan provides full and immediate vesting. It bases benefits on percentages of compensation determined at the age when an employee's participation in a plan begins. The plan is not discriminatory just because the prohibited group of employees are younger than other employees and have benefits determined at higher percentages.[30]

A plan may cover former employees as well as present employees. However, if the plan is amended to provide contributions or benefits that discriminate in favor of certain former employees, the plan will not qualify.

Example. A partnership had a pension plan for the benefit of its present employees. The plan provided for graduated vesting based on years of service. Several of the employees later became partners. The plan was amended to permit the continued increase of the partners' vested interests based on their service as partners. The amended plan did not allow other employees who left the partnership a similar increase in vesting. The plan discriminates in favor of certain former employees who became partners.[31]

Payment of benefits. A plan must specifically provide for the time, manner, and form of benefit payments to employees and their beneficiaries.

The amount to be paid out each year must at least equal the amount found by dividing the employee's interest by the life expectancy that applies. Less may be paid out or no distribution need be made as long as the total amounts paid out by the end of any year are equal to the minimum amounts required to be distributed by that time.[32]

The plan may pay benefits either in a lump-sum or over one of the following periods:

1) The life of the employee; or
2) The lives of the employee and spouse; or
3) A definite period that is no longer than the life expectancy of the employee; or
4) A definite period that is no longer than the joint life and last survivor expectancy of the employee and spouse.

At least 50% of the present value of the total payments to be made to the employee and spouse (or other beneficiary) must be made to the employee. In this way the plan satisfies the requirement that the primary purpose of the plan is to benefit the employee.[33]

Life expectancies cannot exceed the period figured by using:

1) The IRS life expectancy tables; or[34]
2) The life expectancy tables of an insurance company if all payments are made under a contract issued by that company.

These rules on distributions do not apply to any option chosen by an employee before October 10, 1962.[35]

Special Rules for HR-10 Plans

In addition to the rules just discussed, a plan must meet several special rules if the plan includes an owner-employee. These rules do not apply unless at least one owner-employee is in the plan. The owner-employee must consent to be in the plan. The consent may be expressed or implied. Consent is considered made if contributions are made for the owner-employee.

Even if an owner-employee is the only present participant in a plan, the plan must meet all the rules to qualify. For example, it must be a well-written program that has provisions for including other employees when they meet the eligibility requirements.

Because plans must be established by employers and a partnership is considered the employer of the partners, a partner cannot establish a plan for his or her services to the partnership. The partners must consent to having the plan. Each owner-employee can decide whether to be covered. A partner can agree to the plan and still not participate in it if he is an owner-employee.

Limits on employer contributions. Generally, a plan that includes owner-employees must limit the amount of contributions made for any owner-employee to the amount deductible by that person. This is usually 15% of compensation up to $7,500. In the case of a defined benefit plan, these limitations are inapplicable. Regarding deductions, the rules that do apply are contained in section 404(a)(1)(A) of the Internal Revenue Code.

If a plan provides contributions or benefits only for owner-employees, contributions made for any owner-employee may not be more than the amount deductible.

Certain contributions made for an owner-employee for annuity, endowment, or life insurance contracts may be more than the amount deductible. A discussion of the contributions and deductions allowed owner-employees is included later in *Excess Contributions.*

When an employer contribution is made for the owner-employee and either an employee or a self-employed person who is not an owner-employee, the plan may allow voluntary contributions by that owner-employee. The rate of the voluntary contribution by an owner-employee, in proportion to earned income, may not be more than the rate allowed in the plan for other employees.[36]

Prohibited transactions. When an owner-employee covered under the plan, alone or with another owner-employee, controls the business that has the plan, any transaction between that owner-employee (or members of the family[37]) and the plan's trust is a prohibited transaction.

Even if an owner-employee does not control the business, a transaction between the plan and that owner-employee is a prohibited transaction.

A person who engages in a prohibited transaction must pay a 5% excise tax on the amount involved in the transaction. An additional tax of 100% of the amount involved is charged if the prohibited transaction is not corrected within 90 days after IRS mails a notice of deficiency. See the discussion later under *Tax on Prohibited Transactions.*

Coverage requirements. A plan must benefit each employee who has 3 or more years of service.[38] A year of service is a 12-month period in which the employee works at least 1,000 hours starting with the day the employee begins working.[39]

A one-year break in service is a 12-month period in which the employee does not work more than 500 hours. If an employee has a one-year break in service before becoming eligible to join the plan, the plan may disregard any service that was completed before the break in service.[40]

The following employees do not have to be covered under an HR-10 plan even if they have completed 3 or more years of service:

1) Employees in a unit covered by a collective bargaining agreement if retirement benefits were subject to good-faith bargaining between employee representatives and the employer,[41] and
2) Nonresident alien employees who do not have earned income from U.S. sources.[42]

Contributions made for employees who work for more than one employer are based only on the part of the employee's compensation paid by the employer that has the plan.

An annuity and a bond purchase plan established by a partnership may be treated as one plan to determine if the coverage requirement for employees with at least 3 years of service has been met.

Example. A partnership set up an annuity plan covering employees and owner-employees who were under age 72. To provide benefits for an employee over 72, it established a bond purchase plan. The plans may be treated as one to determine if the employee coverage requirements are met.[43]

A partnership that transfers its employees to an unrelated corporation must consider those employees in determining if its profit-sharing plan meets the coverage requirements. This is true if those employees who are subject to the supervision of the partners continue to do the same work they did before the transfer.[44]

A plan with owner-employees may not require a waiting period for employees that is longer than that required for the owner-employees. For example, a new partnership's plan that includes owner-employees must provide immediate coverage for its employees. The plan may not be amended later to remove this requirement for new employees. In other words, the partnership cannot amend the plan 2 years later to require 2 years of service for its new employees.[45]

Continued employment after normal retirement age. A plan with owner-employees must require contributions for other participants who continue employment after the normal retirement age if current contributions are being made for the owner-employees.[46]

The trustee normally must be a bank. However, the trustee need not be a bank if:

1) The funds of the trust are all invested in life insurance company insurance contracts, and
2) All proceeds under those contracts are payable to the employee or the employee's beneficiary, and
3) The plan provides for use of a bank as substitute trustee or custodian if IRS notifies the employer that the trustee has not kept adequate records or filed required information.

The term "bank" means a national or state chartered bank, trust company, or bank corporation. It also includes building and loan associations and federally insured credit unions.

For a trust located in a foreign country, a bank or trust company must be subject to the supervision and examination of governmental authority.[47]

Even if a bank is required as a trustee, the trust may permit others, including owner-employees, to direct trust investments.

An employer may have one or more trusts, custodial accounts, annuity plans, or any combination of these as parts of a single plan. However, if an owner-employee is covered, each trust, custodial account, and annuity plan must meet the requirements that apply to plans with owner-employees.

Contribution formula for a profit-sharing plan. A profit-sharing plan with an owner-employee must have a definite formula for determining employer contributions for employees who are not owner-employees. It must define the profits to be shared. Contributions under the formula may vary from year to year as long as the formula is fixed. The plan may contain variable factors if the amounts to be contributed can be definitely determined each year and cannot be changed by the employer. There is no definite formula if the plan lets the employer vary the percentage of profits to be contributed each year.[48]

Contributions may be geared to profits on a graduated scale, such as on a stated percentage of profits of more than a certain amount. Contributions may also be on the basis of a set percentage of profits minus certain reserves.

A contribution formula is definite if it limits the amount to be contributed for employees, other than self-employed persons and owner-employees, to the same percentage of compensation as the maximum percentage of earned income that may be contributed for the self-employed persons and owner-employees.

A formula is not definite if it requires the contribution of a stated percentage of profits plus additional amounts determined by the employer from time to time. Nor may a formula require the employer to contribute a stated percentage of profits after deducting an amount for unforeseen events that the employer determines necessary.

A definite contribution formula may not be amended except for valid business reasons.[49]

A plan does not have a definite contribution formula if it allows self-employed persons, but not owner-employees, to choose each year the amounts to be contributed for them.[50]

Nonforfeitable rights. If an owner-employee is in the plan, the rights of each employee and self-employed person to the contributions or the benefits from those contributions cannot be forfeited (lost) once the contributions are made.

Employer contributions made for employees cannot later be called excess contributions to have them returned to the employer. This violates the requirement that employer contributions for employees cannot be forfeited once they are made.[51]

Integration with social security. The usual rules for integrating (combining) plans with social security generally do not apply to plans with owner-employees. There are special rules for integrating these plans.

A defined benefit plan may not be integrated with social security.

For a defined contribution plan, self-employment and FICA taxes are treated as employer contributions. A plan with an owner-employee can be integrated with social security only if no more than one-third of the employer contributions are made for owner-employees. The plan can be integrated under special rules that consider only those social security taxes paid by the employer on the maximum amount of wages subject to FICA tax. The earned income of a self-employed person who is not an owner-employee will be treated as wages subject to FICA. The hospital insurance (Medicare) tax is not considered. See the example later that illustrates these rules.

The employer's contribution for an owner-employee must be reduced by the self-employment taxes paid for that person.

If the contributions made for all owner-employees for any tax year are more than one-third of the employer contributions, the plan is not integrated for that year. In addition, contributions must be made to all plan members on a nonintegrated basis. A plan cannot provide that employer contributions are to be made only for years when the integration requirements are met.[52]

Example. Raymond Smith and Harold Tibbs are equal partners in business. They have 11 employees, each with more than 3 years of service. A plan is set up that gives employees with 3 or more years of service immediate rights, which cannot be forfeited, to contributions made for them. The plan calls for contributions of 15% of earned income for owner-employees up to $7,500 and provides for integrating the plan with social security. Since contributions for owner-employees after integration with social security ($3,180) are not more than one-third of net contributions under the plan ($11,414), social security and self-employment taxes may be considered. Employees' wages and partners' earned income are as follows:

	Partners	*Employees*	
	Two	*Six*	*Five*
Earned Income or Wages			
Wages or earned income per person	$20,000	$ 8,000	$ 7,000
Total wages or earned income	40,000	48,000	35,000
Contributions (15% of totals above)	$ 6,000	$ 7,200	$ 5,250
Minus: Amount of SECA or FICA paid by employer*	2,820	2,438	1,778
Net contributions under integrated plan	$3,180	$ 4,762	$ 3,472
Total net contributions			$11,414

*These rates do not include Medicare portion.

Controlled business. If an owner-employee or group of owner-employees control any business, any plan they set up for the controlled business must provide contributions and benefits at least as favorable as the contributions and benefits provided for them under the plan of any business they do not control.

If a plan provides contributions or benefits for an owner-employee who controls the business with the plan, and the owner-employee also controls as owner-employee one or more other businesses, plans must be set up for the controlled businesses. These plans, when taken together, must satisfy the qualification requirements for the employees of all the businesses as if they were a single plan.

Benefits under a profit-sharing plan are not comparable to those under a pension plan. Thus, an owner-employee covered by a pension plan in a business that is not controlled will not satisfy this requirement when a profit-sharing plan is set up for the employees of the controlled business.[53]

Control defined. An owner-employee or group of owner-employees are considered to control a business if they together:

1) Own the entire interest in an unincorporated business, or
2) Own more than a 50% interest of the capital or profits interest of a partnership.

To find if an owner-employee or a group of owner-employees control a business, it does not matter if those persons could be covered under a plan set up for the business.

For example, if an owner-employee has a capital interest of 60% in another business in which there are no personal services, that person controls the business even if no earned income is received from it.

An owner-employee or a group of owner-employees is considered to own any interest in a partnership that is owned, directly or indirectly, by a partnership controlled by that owner-employee or group of owner-employees. An owner-employee or a group of owner-employees control a business only if the owner-employees are covered by the plan.

Example. Elmer Crane owns 50% of the capital interest in both the AB and AC partnerships. If the AB partnership sets up a plan covering Elmer and Carl Jones, neither Elmer nor Carl is considered to control the AC partnership because Elmer does not control either partnership and Carl is not a member of the AC partnership.

Distribution of benefits. A plan with owner-employees must set the time for distribution of an owner-employee's benefits.

Minimum age. A plan with an owner-employee must not pay a benefit to an owner-employee before that owner-employee reaches age 59½, except for disability. Voluntary contributions made by the owner-employee may be paid.

Payment may be made to the estate or beneficiary of a deceased owner-employee before the time the owner-employee would have reached age 59½.

Disability means that you are unable to engage in any substantial gainful activity because of a physical or mental condition. A physician must determine that the condition is expected to result in death or is expected to continue for a long, indefinite time.[54]

If a plan ends early, a deferred annuity may be distributed without causing a premature distribution. The distribution of an owner-employee's interest, or any part of it, after the person reaches age 59½ is determined by the plan.

Example. A plan provides for distribution to be made only when an owner-employer reaches the normal retirement age of 65. Lou Smith, an owner-employee, who will be 59½ next month, is not entitled to a distribution under the plan.[55]

Premature distribution. If a distribution is made prematurely to an owner-employee, even though the plan prohibits it, no further contributions may be made under any Keogh plan by or for that person for 5 years after the distribution is made. In addition, a tax on the premature distribution is charged, as discussed later under *Premature Distributions.*

There is no premature distribution when an annuity contract is transferred from a plan's trust to a bank custodian of another plan that covers the same owner-employee.[56]

There is a premature distribution if a retirement income contract is received by an owner-employee after a change from a qualified trust plan to a nontrust annuity plan and the contract is not converted to an annuity contract within 60 days.[57]

There is a premature distribution when, before reaching age 59½ or becoming disabled, an owner-employee is paid the cash surrender value of a nontransferable annuity contract. It does not matter if the owner-employee later pays this cash to the bank custodian under another plan. The owner-employee has no legal obligation to pay the bank custodian the cash received. It is held by the owner-employee without any conditions until it is deposited with the custodian.[58]

An owner-employee is in constructive receipt of a distribution when a policy loan, or an automatic premium loan, is received under a contract bought as part of a plan. Similarly, an owner-employee has a distribution when a loan is received under a face-amount certificate bought as part of a plan.[59] The amounts credited to a person as a policyholder of a contract are not considered distributions if they are dividends or refunds of premiums and they are used to buy benefits under a policy.[60]

Maximum age. A plan with an owner-employee must begin distributing the owner-employee's entire interest before the end of the year the owner-employee reaches age 70½.

If an owner-employee dies before receiving the entire interest in a plan, there are two ways to distribute the interest:

1) The remaining interest must be distributed to a beneficiary or beneficiaries within 5 years after death, or
2) An immediate annuity must be purchased for and immediately distributed to the beneficiary or beneficiaries within 5 years after death.

However, if at the time of death a distribution had started and is for a certain period no longer than the joint life and last survivor expectancy of the owner-employee and spouse, distribution is not required within 5 years after the death of an owner-employee.

Benefit payments. An employee must receive benefits no later than the 60th day after the end of the year the employee:

1) Ends employment, or
2) Reaches normal retirement age, or
3) Completes 10 years in the plan, whichever is later.

Benefits may not be delayed beyond age 70½ (for owner-employees), or the later of age 70½ or the end of employment (for other employees).

A plan must have a direct statement against premature distributions. It does not matter if state law requires an insurance company to pay the cash surrender value that may be due to the insured or other entitled person when requested. The plan must also have a direct statement of the penalties.[61]

A premature distribution to an owner-employee will not necessarily disqualify the plan for other participants.

Example. George Banks is a sole proprietor who has a plan that includes all employees. He received a premature distribution of his interest. George continued making contributions only for other employees. The restriction against contributions being made by or for George for 5 tax years applies only to George. The plan itself is not affected.[62]

Contributions and Deductions for Self-Employed Persons

Contributions and benefits are limited for self-employed persons. The limits are different for defined contribution plans and defined benefit plans. There are also other limits for either kind of plan.

Defined Contribution Plans

The maximum contribution for owner-employees and the deduction allowed self-employed persons is the lesser of:

1) $7,500, or
2) 15% of the earned income from the business that has the plan.[63]

The limitations above, however, cannot be less than the lesser of:

1) $750, or
2) 100% of the earned income from the business that has the plan.[64]

A contribution may be made in certain situations disregarding the 25% of compensation limit that normally applies to contributions made for persons in defined contribution plans. However, a self-employed person's adjusted gross income may not be more than $15,000. Community property laws are not considered.[65]

Example. John White is a sole proprietor. He earned $500 from self-employment for the year. He figures the contributions to a plan and his deduction as follows:

1) Maximum limit	$7,500
2) 15% of $500 earned income	$ 75
3) Limit ((1) or (2), whichever is less)	$ 75

Because there is a minimum contribution, John's deduction is $500 instead of $75 and is figured as follows:

1) Allowable minimum contribution	$ 750
2) 100% of earned income	$ 500
3) Minimum contribution ((1) or (2), whichever is less)	$ 500

Carryover deductions. Contributions for self-employed persons that are above the limits for a year may be carried forward to later years. However, the contributions above the limits for a year are subject to a 6% excise tax on excess contributions. This is discussed later under *Excess Contributions.*

The contribution for a later year plus the carryover contribution may be deducted up to $7,500 or 15% of earned income, whichever is less, of a self-employed person for that later year.[66]

If the contributions are made to two or more plans, these plans are treated as one in applying the limit.[67]

If contributions are made to a defined benefit plan and a defined contribution plan, excess contributions for that year also may be carried forward to later years and deducted. The deduction in later years of both the contribution for the year and the contribution carryover from earlier tax years may not be more than either $7,500 or 15% of the earned income, whichever is less.[68]

Combination of two or more plans. When contributions are made to two or more plans for a self-employed person, the combined deduction may not be more than $7,500 or 15% of earned income, whichever is less. This limit does not apply to contributions made for an employee who is not self-employed in the business that has the plan.[69]

If the limit for contributions made for self-employed persons to two or more plans reduces the amount deductible by each employer, a formula is used to find the part of the nondeductible contribution for each employer. The formula for each employer is:[70]

$$\text{Amount deductible} \times \frac{\text{Earned income from employer}}{\text{Earned income from all businesses with plans}}$$

A self-employed person who uses the minimum contribution rule and has contributions made to two or more plans must use all earned income to figure the limit on contributions.[71]

Defined Benefit Plans

A defined benefit plan must limit the benefits for self-employed persons instead of limiting contributions. The plan also must prohibit the accrual of a benefit that is more than the maximum for a year. Two kinds of defined benefit plans are discussed here. They are career average pay plans and final average pay plans.

The following discussion gives only the highlights of the requirements defined benefit plans must meet to be qualified. More complete information can be found in the proposed regulations concerning defined benefit plans for self-employed persons.

The Internal Revenue Service has approved three master and prototype defined benefit plans. These plans contain representative language that satisfies legal requirements. They are available for public inspection and reproduction at the seven IRS regional Freedom of Information Reading Rooms and at the IRS Reading Room, Room 1569, 1111 Constitution Ave., N.W., Washington, DC 20224.

Career average pay plans. Under a career average pay plan, the basic benefit that accrues for any year of participation may not be more than a maximum basic benefit for a self-employed person.

Basic benefit. The basic benefit of an employee is the benefit a plan provides under certain conditions. The plan must have no additional benefits and employees must not contribute. The basic benefit must be in the form of a straight life annuity, and it must begin at age 65, or 5 years after the participant's current period of participation began, whichever is later.[72]

The maximum basic benefit is:

1) The annual compensation (no more than the compensation base for the year), multiplied by
2) The statutory percentage adjusted for the year.[73]

The annual limit on the maximum basic benefit for an employee is $3,250 (6.5% of $50,000).

Compensation is the earned income of a self-employed person.[74]

The current period of participation is any period of consecutive plan years of participation beginning with the first day of the first year in that period and ending with the last day of the last year in the period.[75]

The compensation base is the highest level of an employee's annual earned income that may be considered in figuring benefits.[76] This may not be more than $100,000.

A plan year of participation is a plan year when a participant earned a benefit.[77] A participant earns a benefit if 1,000 hours of service are completed in the plan year.

Plan participation starts at the beginning of the first plan year of participation in the plan. If an individual has accrued benefits from an earlier period of participation, that past service is not considered for the current period of participation.[78]

The statutory percentage for an employee in a plan year is on the following table opposite the employee's age. Use the employee's age when the current period of participation began.

The statutory percentage may change periodically because of changes in prevailing interest and death rates.[79]

An employee's statutory percentage at a given date, such as when participation began, is determined using the age on the employee's birthday on or before the given date.[80]

Age	Statutory percentage
30 or less	6.5
31	6.3
32	6.0
33	5.8
34	5.6
35	5.4
36	5.1
37	4.9
38	4.8
39	4.6
40	4.4
41	4.2
42	4.1
43	3.9
44	3.8
45	3.6
46	3.5
47	3.4
48	3.2
49	3.1
50	3.0
51	2.9
52	2.8
53	2.7
54	2.6
55	2.5
56	2.4
57	2.3
58	2.2
59	2.1
60 or over	2.0

Example 1. John White is self-employed. He joins a defined benefit plan at age 30. The plan provides benefits on income up to $50,000 in the form of a single life annuity beginning at age 65 with no additional benefits. If John's income for the first year is $20,000, the maximum basic benefit is $1,300 (6.5% of $20,000). The percentage for that year is for age 30, the age when John begins participating.

For the next 4 years, John's income stays at $20,000. John's maximum benefit for each of these years is still $1,300. The statutory percentage is still 6.5% for age 30 when he began participating, even though he is older.

After 5 years, John leaves the plan. He starts participating again at age 50. The first year after his return, John earns $30,000. His maximum benefit for the year is $900 (3% of $30,000). The statutory percentage is for age 50 when his current period of participation began, not age 30. If John's income stays at $30,000 for 4 more years, John's maximum benefit for each of these years stays at $900.

Example 2. Ray Blue is self-employed. He is in a defined benefit plan. In 1980, Ray's total accrued annual benefits are $13,000. Ray's total maximum basic benefit is $13,500. However, the plan accrued an annual benefit for Ray of $1,800 for 1980 when his maximum basic benefit was $1,625. This disqualifies the plan for 1980. The limit must be satisfied each year, even though total benefits may satisfy the limits.

Fully insured plans. If a plan invests only in insurance or annuity contracts, the statutory percentages must be adjusted by using special tables based on sex and age.[81]

Voluntary employee contributions. The maximum basic benefit does not need to be adjusted for voluntary contributions. A plan can provide a benefit equal to the maximum basic benefit plus the benefit for voluntary contributions. These contributions must be accounted for separately.[82]

Mandatory employee contributions. The employee's total accrued benefit must be divided between the part from mandatory employee contributions and the part from employer contributions. Voluntary contributions are not considered in the total accrued benefit.

Integration with social security. If a defined benefit plan provides contributions or benefits for owner-employees, the plan will not qualify if the plan offsets its benefits by the benefits provided under social security or similar laws.[83]

Final average pay plans. Generally, the rules that apply to career average plans also apply to final average plans. However, very complex rules apply to final average plans, such as the limit on maximum benefits. These rules are set forth, along with a worksheet, in the regulations. See also, *Maximum $100,000 limit.*

Other Limits

In addition to the specific limits for defined contribution and defined benefit plans, there are other limits that must be met for a plan to qualify.

Maximum $100,000 limit. A plan that covers one or more self-employed persons may not consider more than the first $100,000 of earned income of any employee.

An employer who maintains more than one plan for the same business must consider all the plans as a single unit.[84]

In addition, if an employer controls one or more plans in separate businesses, the plans must be considered as one in determining the $100,000 limit.[85]

Integration with social security. The $100,000 limit must be determined without any adjustments to contributions or benefits because of integration with social security.[86]

Nondiscrimination requirement. The income for each self-employed person is assumed to be $100,000 rather than the income actually received in a year in determining if the rate of contributions discriminates in favor of highly compensated employees.[87]

This applies to a defined contribution plan that covers self-employed persons and to a year in which the income of any employee covered is more than $100,000.[88]

Example. Judy White is self-employed. She set up a defined contribution plan that covers her and two employees. In 1979 Judy had earned income of $150,000 and the two employees had less than $100,000. If Judy wishes to contribute $7,500 to the plan for her, she must contribute to the employees' accounts amounts at least equal to 7½% of their earnings.

Voluntary contributions. When an employer makes a contribution for an owner-employee and either an employee or a self-employed person who is not an owner-employee, the plan may permit voluntary contributions by the owner-employee. The rate of voluntary contributions in proportion to earned income may not be more than the rate permitted in the plan for other employees.

The limit on nondeductible voluntary contributions that an owner-employee may make for any year is the least of the following:

1) $2,500,
2) 10% of the earned income from the business with the plan, or
3) The amount of the contribution that would be contributed by the owner-employee if it were made at the rate permitted to be made by employees other than owner-employees.

No voluntary contributions may be made if a plan has no employees other than owner-employees.

Repayment of loan. Any amount paid either directly or indirectly by an owner-employee to repay a loan that was treated as received from a qualified trust or plan is considered a voluntary contribution.[89]

Insurance protection. Employer contributions to purchase life, health, accident, or other insurance under the plan are not considered for the contributions limit.[90]

The amounts are considered in the limit if the 3-year averaging method that applies to insured plans funded on a level premium basis is used. This is discussed under *Excess Contributions*.

Excess Contributions

An employer who has a plan that covers any self-employed persons is subject to a 6% excise tax on excess contributions. Excess contributions are figured differently for defined contribution and defined benefit plans.

Figuring Excess Contributions

Excess contributions are the total of the following reduced by correcting distributions (discussed later) made in all earlier years after 1975:

1) Excess voluntary contributions by the owner-employee, and
2) Excess contributions to defined benefit plans, and
3) Excess contributions to defined contribution plans.[91]

Excess voluntary contributions are figured as follows:

Owner-employee voluntary contributions for the year	$
Minus voluntary contributions permitted for the year	
Excess (if any)	$
Plus excess contributions for an earlier year	
Total excess voluntary contributions	$

Example. Robert Barnes is self-employed. He had earned income of $50,000 in 1979. In 1979 Robert made a voluntary contribution of $4,000. There were no excess voluntary contributions in 1978. Robert figures the excess voluntary contribution as follows:

Voluntary contribution for 1979	$ 4,000
Minus voluntary contributions permitted in 1979 (lesser of $2,500 or 10% of $50,000)	2,500
Excess	$ 1,500
Plus excess voluntary contributions for earlier years	none
Total excess voluntary contributions	$ 1,500

Excess contributions to defined benefit plans are the contributions by the employer after 1975 if:

1) At the end of the year the plan is fully funded, and
2) The contributions were not deductible in any earlier year.

Excess contributions to defined contribution plans are the part of the contributions by the employer after 1975 that was not deductible.

Example. JMO Partnership has a defined contribution plan. In 1979 the partnership contributed $13,000 for its employees. In 1978 the partnership contributed $2,000 more than the allowable deduction. The $2,000 was an excess contribution in 1978. No corrective action was taken. The plan does not provide for any voluntary contributions.

Total contributions for 1979		$13,000
Minus deduction allowable for 1979—		
1. owner-employee ($50,000 × 15%)	$7,500	
2. employees ($25,000 × 15%)	3,750	
Total		11,250
Excess contributions for 1979		$ 1,750
Plus excess contributions for 1978		2,000
Total excess contributions for 1979		$ 3,750

Tax on Excess Contributions

An excise tax of 6% is charged on the excess contributions figured at the end of the tax year. The tax must be paid by the employer.[92]

An excess contribution made in one year is subject to tax in later years unless a correcting distribution is made.

A correcting distribution depends on the contribution made. For excess voluntary contributions, the correcting distribution is the amount of the excess contribution returned to the owner-employee.

For excess contributions to defined benefit plans, the correcting distribution is the amount of the nondeductible contribution returned to the employer.

For excess contributions to defined contribution plans, the correcting distribution is the amount of the excess contribution returned to the employer or, for a profit-sharing plan, to the employee for whom the contribution was made.

Contributions for Insurance

Excess contributions that are used (either directly or through a trustee) to pay premiums for annuity, endowment, or life insurance policies are not taxed.[93]

Employer contributions to pay premiums for any owner-employee may not be more than $7,500 a year for life, accident, health, or other insurance.[94]

The limit of 25% of compensation on annual contributions for owner-employees does not apply when insurance is purchased if:

1) The annual addition to the plan for the owner-employee is that contribution only, and
2) The owner-employee is not a participant during the year in a defined benefit plan maintained by that employer.

The plan will not be discriminatory if contributions made for employees are limited to 25% of compensation.[95]

Although employer contributions must be made under a qualified plan, certain qualification requirements are modified.[96] A plan may not be disqualified if a contribution is made for an owner-employee by the employer in a year the owner-employee has no earned income.[97]

Employer contributions must be to pay premiums for a policy on the life of the owner-employee. All proceeds of the policy must be payable directly or through the trust to the owner-employee or a beneficiary.[98]

Employer contributions made for the owner-employee for any year and used to pay premiums must not be more than the average of the amounts deductible by the employer for the owner-employee for the most recent 3 years. The last of the 3 years must have ended before the latest policy was bought or changed to provide more benefits. If the owner-employee had no earned income for those 3 earlier years, in averaging the amounts deductible, use only the years the owner-employee had earned income in that business.[99] Years before a plan was set up may be used.[100]

To find the average for the 3 years, use the same limit on deductible contributions that is used for the current year.[101]

The amount of contributions for insurance protection may not be more than $7,500 a year for each owner-employee.[102]

The nondeductible part of the employer contributions is treated as voluntary contributions by the owner-employee in finding if the tax applies to other sources of contributions. Thus, an excess contribution may not be from employer contributions but may be from voluntary contributions by owner-employees.[103]

Example 1. Ed Green is self-employed. He had earned income of $25,000 in 1979. The contribution to his plan pays the premiums on life insurance for him and his employees. For 1979, $5,800 was paid as a premium on Ed's life insurance. Ed's earned income for the preceding 3 tax years was: 1976—$25,000; 1977—$50,000; 1978—$45,000.

It would appear that Ed is liable for the tax on excess contributions for 1979, since the contribution of $5,800 is more than the maximum deduction of $3,750 (15% of $25,000). However, because of the exception for insurance coverage, he finds that he is not liable. The $5,800 contribution is not more than the $6,000 average amount deductible for the 3 preceding years.

1976—15% of $25,000	$ 3,750
1977—15% of $50,000	7,500
1978—15% of $45,000	6,750
Total	$18,000
Average ($18,000 divided by 3 years)	$ 6,000

The excess of $2,050 ($5,800 minus $3,750) is considered a voluntary contribution.

Example 2. Assume that in Example 1 the contribution was $6,200 instead of $5,800. Since the exception would not apply, any excess contribution that is subject to the tax is found as follows:

1) Part of contribution that is more than the maximum amount deductible ($6,200 minus $3,750)	$ 2,450
2) Minus maximum voluntary contribution permitted by owner-employee (lesser of $2,500 or 10% of $25,000)	2,500
3) Excess contribution	None

Filing Requirements

The 6% excise tax is figured on Form 5330, *Return of Initial Excise Taxes Related to Pension and Profit-Sharing Plans.*

When to file. The return must be filed by the last day of the 7th month after the end of the employer's tax year.

An extension of up to 6 months to file Form 5330 may be granted on or before the due date. To request the extension, use Form 5558, *Application for Extension of Time to File Certain Employee Plan Returns.*

Where to file. The return should be filed with the Internal Revenue Service Center where your Form 1040 is filed.

Contributions for Employees

The amount deductible for contributions made for employees is figured as if they were the only participants in the plan.[104]

Contributions to a Profit-Sharing Plan

The amount that may be deducted by an employer for contributions to a profit-sharing plan for employees may not be more than 15% of their compensation.[105]

Contribution less than amount deductible. If contributions to a plan in any year are less than 15% of compensation, the difference between the amount contributed and 15% of compensation may be carried forward and deducted when paid in later years in order of time. The carryover amount deductible in that later year may not be more than 15% of compensation in that year.

The total of the 15% current year limit and the 15% carryover limit in the later year may not be more than 25% of the compensation in that later year.

Example. John Green is self-employed. He contributed $1,000 to a profit-sharing plan for his employees for 1978. The total paid the employees in 1978 was $10,000. In 1979 John contributed $3,500 to the plan for his employees. This included $500, the balance of 1978 contributions, and $3,000 contributions for 1979. The employees' pay for 1979 was $20,000. John figures the amount he can deduct for each year as follows:

1978	
15% limit for 1978 (15% of $10,000)	$1,500
Contribution	1,000
Carryover amount	500
Amount deductible	1,000
1979	
15% limit for 1979 (15% of $20,000)	$3,000
1978 carryover amount	500
Amount contributed	3,500
Amount deductible	3,500
Maximum 25% limit (25% of $20,000)	$5,000
1979 carryover amount	-0-

Contributions of more than the amount deductible. If the contributions for employees are more than the amount deductible for a year, the excess is carried over to later years in order of time. The amount deductible, which includes both the contribution for the current year and the excess from earlier years, may not be more than 15% of compensation.

Example. In 1978, Ray Brown contributed $4,000 to a profit-sharing plan for his employees. Their pay for the year was $20,000. In 1979 Ray contributed $3,500 to the plan for his employees. Their pay for 1979 was $30,000. Ray figures his deductions as follows:

1978	
Contribution	$4,000
15% limit for 1978 (15% of $20,000)	3,000
Carryover to later years	1,000
Deduction	3,000
1979	
Contribution	$3,500
Carryover from 1978	1,000
Total	$4,500
15% limit for 1979 (15% of $30,000)	$4,500
Deduction	$4,500

Contributions to Both a Pension and a Profit-Sharing Plan

The amount deductible for contributions paid to both a pension and a profit-sharing plan for employees in a year may not be more than the greater of:[106]

1) 25% of compensation, or
2) Contributions up to the amount needed to satisfy the minimum funding standard[107] for the year.

Contributions that are more than the amount deductible. Contributions to two or more pension and profit-sharing plans of more than the amount allowable may be deducted in later years in order of time. The carryover plus the contribution for the later year may not be more than 25% of compensation in that year.

If no employee is a beneficiary under more than one trust or a trust and an annuity plan, this discussion does not have the effect of reducing the amount otherwise deductible.

When Contributions Are Considered Made

An employer is considered to have made a contribution to a plan on the last day of the previous year if the payment is for that year and if certain conditions are met. The payment must be made by the due date, including extensions, of the tax return for the year.[108]

The employer must elect to have this apply. The election, once made, cannot be revoked.[109]

The election is made if:

1) The contribution is made by the due date, including extensions, for filing the tax return, and
2) A deduction is taken for the contribution on the tax return for the year. If a contribution is made by a partnership, it must be deducted on Schedule K of the partnership return.

No formal statement is needed to make the election.[110]

The payment will be considered for the previous year if:

1) It is treated as the plan would treat a payment actually received on the last day of the previous year, and
2) Either of the following two conditions is satisfied—

a) The employer designates in writing to the plan administrator or trustee that the payment is for the previous year, or

b) The employer takes the deduction on the tax return for the previous year. If the contribution is by a partnership, the contribution must be deducted on Schedule K of the partnership tax return.[111]

Funding a Plan

A plan must be funded and there are several ways to do it. A trust may be established to invest the funds of a plan. An annuity plan may purchase an annuity contract with incidental life insurance on the participants. Face-amount certificates, which are treated as annuity contracts, may be bought by the employer, trust, or custodial account directly from an insurance company. A plan also may be funded with U.S. Retirement Plan Bonds. A custodial account may be established to invest the funds.[112]

Insurance Contracts

Individual or group insurance contracts with only incidental life insurance protection may be used in an annuity plan. An annuity plan without a trust may be funded by retirement income contracts.[113]

Incidental life insurance. In a defined benefit plan funded with insurance contracts, the life insurance is considered incidental if it is no more than 100 times the monthly annuity, such as $1,000 of life insurance for each $10 of monthly annuity. Generally, a defined benefit plan with self-employed persons may not have retirement benefits that are derived solely from ordinary life insurance contracts or similar life insurance contracts with death benefits of more than 100 times the monthly retirement income.[114]

In a defined contribution plan, life insurance is considered incidental if no more than 25% of the employer's contribution is used to buy life insurance. For example, if term life insurance is used, the premium cannot be more than 25% of the employer's contribution. If ordinary life insurance, in which half of the premium goes toward insurance protection and half goes toward a cash reserve, is used, the limit is 50%. If both are used, the premium for term insurance, plus half the ordinary life premium, cannot be more than 25%.

For retirement income contracts, the insurance is considered incidental if the death benefit before retirement is no more than 100 times the monthly annuity after retirement.

Face-Amount Certificates

A face-amount certificate is treated like an annuity contract. These certificates may be bought by the employer, trust, or custodial account directly from the insurance company.[115]

Certificates and annuity contracts must not be transferable when held by anyone other than a trustee. The certificate or contract must state that it is not transferable.

When a group certificate or contract is bought, the participants' interests must not be transferable. A certificate or contract is transferable if the owner can transfer any part of the interest in it to anyone other than the issuer.

An employee may designate a beneficiary or choose any settlement option under the plan.[116]

Bond Purchase Plans

A plan may be funded with U.S. Retirement Plan Bonds.[117] A bond purchase plan must meet the coverage, nondiscrimination, and most other qualification requirements.[118]

U.S. Retirement Plan Bonds pay interest of 6½% a year compounded semiannually. They may be purchased in the name of the participant only.

The bonds have no set maturity date but they do stop paying interest 5 years after the death of the person in whose name they are bought. They may not be transferred and they cannot be forfeited. They may not be cashed by the employee before age 59½, except for disability. They may be cashed by the beneficiary after the employee dies.

Bonds may be bought in $50, $100, $500, or $1,000 denominations. The most that can be bought for any person in a year is $10,000.

Bonds may be bought or cashed at any Federal Reserve Bank branch or at the Office of the Treasurer of the United States.

Bonds may be bought as investments under any qualified pension or profit-sharing plan. Their use is not limited to plans with self-employed persons.

A simplified bond purchase plan form is available for self-employed persons who want to set up or amend a plan. Complete Form 4578, *Application for Determination of Bond Purchase Plan that Includes Self-Employed Individuals,* to establish a bond purchase plan. You may get this form from any Internal Revenue office.[119] Do not file it with the Internal Revenue Service; keep it for your records.

Custodial Accounts

A plan may use a custodial account with a bank instead of a qualified trust. One or more custodial accounts may be used as part of a single plan or with one or more annuity plans of the employer, if each plan separately qualifies, or all plans qualify as one.[120]

Credit unions, industrial loan companies, savings and loan associations, and certain other financial institutions may act as trustees. However, the trust assets must be invested only in deposits of the trustees. Deposits handled by the trustees must be insured by an agency of the United States or a state.

A custodial account and annuity contract are considered qualified trusts. For a custodial account with assets in a bank or insured credit union, each must show that it complies with the IRS trustee responsibilities.[121] The person holding the assets of the account or holding the contract is treated as the trustee.

Investment in mutual funds. If investments are made in mutual funds and a stock certificate is not issued, the mutual fund may issue a confirmation to the custodian. The confirmation is the purchaser's evidence of owning the stock. When a distribution is made from a custodial account, a new confirmation is given to, and in the name of, the recipient, who then has all the rights of a shareholder.[122]

Trust for Owner-Employee Only

A plan for a self-employed person that is funded only by buying annuity or other insurance contracts with incidental benefits may use a trustee arrangement. An owner-employee may be designated as the trustee. However, if the owner-employee is also the only beneficiary of the trust, the contracts bought for and held by the owner-employee as the trustee must not be transferable.[123]

Deduction for trustees' fees. Trustees' fees paid by a self-employed person to maintain a plan are deductible in addition to contributions under the plan.[124]

Premature Distributions

A plan must not allow an owner-employee to receive a distribution from the plan before age 59½ unless the owner-employee is disabled. If an owner-employee receives a premature distribution, a penalty will be charged and the owner-employee may not participate in the plan for 5 years.[125]

An owner-employee is allowed to withdraw voluntary contributions without penalty.

The penalty for a premature distribution is 10% of the amount received that is included in the owner-employee's income.[126]

A person is disabled if he or she is unable to engage in any substantial gainful activity because of a physical or mental condition. The condition must have lasted or be expected to last for a long period or the condition must be expected to lead to death.[127]

A condition that can be corrected is not a disability. The person will not be considered disabled if, with reasonable effort and safety, the condition can be lessened so that the person can engage in substantial gainful activity.[128]

Certain statements must be attached to the owner-employee's tax return when the owner-employee receives a distribution because of disability.[129]

For the first year, a doctor's statement about the disability must be attached. The owner-employee must also attach a statement explaining the effect of the mental or physical condition, why he or she is unable to engage in substantial gainful activity, and the date the condition began.

In later years, the taxpayer may attach a statement saying that the condition has not lessened substantially and that it still affects engaging in any substantial gainful activity.

Amount to include in income. The following must be included in income as premature distributions in figuring the 10% penalty:[130]

1) Amounts received by the owner-employee before age 59½ that are from contributions paid by the employer, including the increase in value for those contributions (Increases in value from the owner-employee's voluntary contributions made while an owner-employee are also included.), and
2) Amounts that are more than the owner-employee's benefits under the plan formula, and
3) Amounts subject to transitional rules from certain employer contributions made before 1976.

Amounts not to include in income. The following are not included in income in figuring the 10% penalty:[131]

1) Amounts received because of disability,
2) Dividends or similar distributions received by the owner-employee as a policyholder of an annuity, endowment, or life insurance contract, and
3) Amounts from contributions (and increases in value) made while the recipient was not an owner-employee.

Example. Harry Baker was a member of the ABC partnership. The partnership had 9 partners. He was in the partnership's profit-sharing plan that was started in January 1974. Harry's tax year and the partnership's and plan's tax year is the calendar year. From 1974 through 1976, Harry was an owner-employee. In January 1977 two new partners were admitted to the partnership. When they entered, all partners had a 1/11th interest in the partnership. Harry was no longer an owner-employee. In January 1979, when he was 50 and not disabled, he sold his interest in the partnership. Harry received a total distribution of $54,000 from the plan. This violated the plan provision that prohibited distribution before age 59½. The $54,000 was from the following:

Year	*ABC's Contribution for Harry*	*Increase in Value of ABC's Contribution*
1979	$ 0	$ 0
1978	7,500	900
1977	7,500	4,000
1976	7,500	1,800
1975	2,500	1,200
1974	2,500	1,300
	$27,500	$9,200

Year	*Harry's Voluntary Contribution*	*Increase in Value of Harry's Contribution*
1979	$ 0	$ 0
1978	2,500	300
1977	2,500	1,300
1976	2,500	700
1975	2,500	1,200
1974	2,500	1,300
	$12,500	$4,800

Total of all columns ($27,500 + 9,200 + 12,500 + 4,800) $54,000

The part of the distribution that is premature is $20,000, figured as follows:

ABC's contributions for Harry made when he was an owner-employee:

1976	$7,500	
1975	2,500	
1974	2,500	
Total		$12,500

Increase in value of ABC's contributions:

1976	$1,800	
1975	1,200	
1974	1,300	
Total		$ 4,300

Increase in value of Harry's voluntary contributions made while he was an owner-employee:

1976	$ 700	
1975	1,200	
1974	1,300	
Total		$ 3,200
Total distribution subject to penalty		$20,000

The contributions made for Harry for 1977 and 1978 (including the increase in value) are not subject to the penalty, since they were made when Harry was not an owner-employee. The same is true for the increase in value from Harry's voluntary contributions. Harry's voluntary contributions for 1974 are not subject to the penalty, since they were received after September 2, 1974.

Dividing the increase in value. The increase in value from an employer's contributions for a person while an owner-employee and while not an owner-employee may be found by keeping separate accounts or an accounting that shows the actual increase from the contributions.[132] The following method may also be used.

When a person is in a plan both as an owner-employee and a nonowner-employee, the increase in value from contributions made while an owner-employee may be found by multiplying the total increase in value in the account by the following fraction:[133]

1) The numerator is the contributions made for the person as an owner-employee, weighted for the number of years each contribution was in the plan, and
2) The denominator is the total contributions made for the person, weighted for the number of years each contribution was in the plan.

Contributions are weighted for the number of years in the plan by multiplying each by the number of years it was in the plan. If the person received an earlier distribution from the account, an adjustment must be made to show that distribution.

Example. John Ellis was a member of the OPQ partnership and a participant in the profit-sharing plan that was started in 1973. John's interest in the partnership was less than 10% until January 1978 when he got an interest of more than 10%. He continued in the plan until 1982. In 1982, before reaching 59½, John withdraws his interest in the plan. He is not disabled. His interest is $15,000, $9,600 contributions and $5,400 increase from the contributions. The part of the increase from contributions while John was an owner-employee is $667.80, figured as follows:

Years	Contribution	*Years Contribution in Plan*	*Contribution Weighted in Plan*
1982	$1,000	0	$ 0
1981	800	1	800
1980	1,200	2	2,400
1979	600	3	1,800
1978	200	4	800
1977	400	5	2,000
1976	2,000	6	12,000
1975	1,000	7	7,000
1974	1,500	8	12,000
1973	900	9	8,100
Total	$9,600		$46,900

Weighted contributions as owner-employee (1978-1982) = $5,800

Total weighted contributions = $46,900

$$\$5{,}400 \times \frac{\$\ 5{,}800}{\$46{,}900} = \$667.80$$

Order of distribution. If a person participates in a plan as both an owner-employee and a nonowner-employee, the distributions are considered received in the following order:[134]

1) Excess contributions,
2) Employee contributions, and
3) Employer contributions, not included in (1), including the increase in value from the employee's as well as the employer's contributions.

This order of distribution applies to distributions that are less than total distributions.

Amounts Considered Received

Certain amounts are considered to be received by an owner-employee even though no distribution is actually made.

When an owner-employee assigns or pledges (or agrees to assign or pledge) any part of an interest in a trust or of any value of an annuity, the owner-employee treats that part as received during the year as a distribution from the trust or under the annuity.[135]

If an owner-employee received, either directly or indirectly, an amount from an insurance company as a loan under a contract bought by a trust as part of an annuity plan, the owner-employee treats the amount as received under the contract.[136]

An owner-employee is considered to have received an amount under a contract if a premium, which is late, is paid by the insurance company in the form of a loan against the cash surrender value of the contract.

Amounts an owner-employee receives from the issuer of a face-amount certificate as a loan under a certificate purchased as part of a trust or plan are considered received.

Income Tax on Benefits

The tax treatment of the benefits received by a participant after age 59½ from a plan depends on what type of benefits are received. The benefits are taxed either as an annuity or as a lump-sum distribution.

An annuity is periodic income received for a set period of time or for the life of the recipient. A survivor may receive benefits after the death of the recipient.

If an annuity is received, it may be paid by the plan or by an insurance company. To figure the tax treatment of an annuity, the recipient's investment in the contract or what is considered the recipient's cost must be determined. This amount will not be taxed under any method of reporting the annuity.

Investment in the contract. For self-employed persons, the investment in the contract is the voluntary contributions made to the plan. Amounts deducted as contributions on behalf of self-employed persons are not included. Contributions previously distributed to the self-employed person are also not included.

Reporting annuity in income. Two rules are used for reporting annuity income, the Three-Year Rule and the General Rule.

Three-Year Rule. If a self-employed person can recover his or her cost (investment in the contract) within three years after the first payment is received, the Three-Year Rule must be used. Amounts received are not taxed until after the investment in the contract (cost) is recovered.[137]

Example. Mary Green, a self-employed individual, retired on January 1, 1978, and is to receive an annuity over her life. On the date of her retirement, she was 65 years of age. Her investment in the contract is $20,000. Mary will receive $12,000 annually, and she determines that her annuity income will be fully excluded in 1978, and excluded to the extent of $8,000 in 1979, figured as follows:

1978		
Amount received		$12,000
Less		
Investment in contract	$20,000	
Reduced by amount excluded in prior years	-0-	
Excess		$20,000
Taxable portion of annuity		$-0-
1979		
Amount received		$12,000
Less		
Investment in the contract	$20,000	
Reduced by amount excluded in prior year	12,000	
Excess		8,000
Taxable portion of annuity		$ 4,000

Although amounts are excluded in 1978 and 1979, all amounts involved must be reported on Schedule E, Form 1040. For each year after 1979, the full amount received is taxable.

General Rule. This applies to all annuity payments except in cases when the employee or self-employed person's voluntary contributions will be recovered within 3 years. In figuring the amount taxable, the following must be determined:

1) Investment in the contract (defined earlier);
2) Expected return; and
3) Taxable part of annuity.[138]

The ***expected return*** is the total amount expected to be received, or estimated to be received under the contract.

For a fixed period annuity, the expected return is determined by multiplying the fixed number of years or months for which payments are to be made by the amount of payment specified for each period.

For a life annuity, the expected return is found by multiplying the amount of the annual payment by a multiple based on life expectancy as of the annuity starting date. The tables for this computation may be found in Publication 575, *Pension and Annuity Income*, or may be obtained at your local Internal Revenue office.

To find the ***taxable part of an annuity,*** you first figure the portion of the income to be excluded by dividing the investment in the contract by the expected return. The percentage determined remains the same as long as the annuity is received, regardless of whether the expected return is exceeded.

Next, multiply the annuity income received during the year by the percentage already computed. The result is the portion of the annuity that is not taxable; since it represents a return of investment. The taxable portion is found by deducting the excludable portion from the total annuity income received.

Example. John White, a self-employed individual, retires at the age of 65 and is to receive a life annuity of $10,000 annually. His investment in the contract representing voluntary contributions, is $30,000. The applicable multiple for his age (male age 65) is 15.0 as shown in Table 1 (Publication 575). His expected return is $150,000 (15 × 10,000). The investment in the contract of $30,000, divided by the expected return of $150,000 equals 20%, the percentage to be excluded from gross income. Each year, John will exclude $2,000 (20% × $10,000) and consider $8,000 as income as long as payments are received.

A lump-sum distribution is treated differently. It may be taxed partly as ordinary income and partly as capital gain subject to the 60% capital gain deduction. In addition there is a special 10-year averaging method that treats certain parts of the lump sum as though it were received and taxed over a 10-year period.[139]

Publication 575 describes in detail all the methods used to figure the taxable and nontaxable parts of an annuity. It also describes the tax treatment of lump-sum distributions and the use of the special 10-year averaging method.

Tax on Prohibited Transactions

A tax is charged on prohibited transactions between a plan and an owner-employee. The initial tax is 5% of the amount involved in the transaction for each year (or part of the year) in the tax period.[140]

The owner-employee who takes part in the transaction is liable for the tax. If more than one person is liable for the tax, all are jointly and individually liable.

Additional tax. When an initial tax is charged and the transaction is not corrected within the correction period, an additional tax of 100% of the amount involved is charged.

The amount involved in a transaction is the money and fair market value of property received, or the money and fair market value of property given, whichever is greater. If services are performed, the amount involved is the excess compensation given or received.

To figure the initial tax, the fair market value is determined on the date of the transaction.

To figure the additional tax, the fair market value is the highest fair market value during the correction period.

The tax period begins on the day of the transaction. It ends on the day IRS mails a notice of deficiency, or the day that correction of the transaction is completed, whichever is earlier.

A correction is made by undoing the transaction as much as possible without placing the plan's financial position in a worse situation than if the owner-employee were acting under the highest standards for a trustee or custodian.

The correction period begins on the day of the transaction and ends 90 days after IRS mails a notice of deficiency for the 100% additional tax. The correction period is extended if a petition has been filed with the Tax Court or if an extension is granted by IRS for a reasonable time necessary to correct the transaction.

Prohibited Transactions

A prohibited transaction is usually any direct or indirect:

1) Sale, exchange, or lease of any property between a plan and a disqualified person,
2) Lending of money or other extension of credit between a plan and a disqualified person,
3) Furnishing of goods, services, or facilities between a plan and a disqualified person,

4) Transfer to, or use by or for the benefit of, a disqualified person of the income or assets of a plan,

5) Act by a disqualified person who is a fiduciary so that the individual deals with the income or assets of the plan in his or her interest or own account, or

6) Receipt of any consideration by a disqualified person for his own personal account when that person is a fiduciary and deals with any party in a transaction involving the income or assets of the plan.

In general, for these purposes, the owner-employee is a fiduciary and thus a disqualified person.

An owner-employee may receive any benefit to which he or she is entitled as a participant or beneficiary in the plan, as long as the benefit is figured and paid in the same way the terms of the plan are applied to all other participants and beneficiaries. A distribution may be made by a trustee of the assets of a trust according to the terms of the plan.

A transaction is indirect between a plan and an owner-employee if the transaction involves:

1) A member of the owner-employee's family (whole or half-blood brothers and sisters, spouse, ancestors, and lineal descendants), or

2) A corporation controlled by the owner-employee who owns, directly or indirectly, 50% or more of the total voting stock, or 50% or more of the total value of all classes of stock of the corporation.

Reporting a Prohibited Transaction

Form 5330 must be filed by any owner-employee who takes part in a prohibited transaction for each tax year (or part of one) in the tax period. The tax paid with the return is the 5% initial tax. The 100% additional tax assessed by IRS is not reported on a form.

The return must be filed by the last day of the 7th month after the end of the owner-employee's tax year. An extension of time to file up to 6 months may be granted if the request for extension is made in writing by the due date for filing the return. Form 5558 may be used to request the extension.

The return should be filed with the Internal Revenue Service Center where the income tax return of the owner-employee is filed.

Determination and Opinion Letters

The Internal Revenue Service will issue a determination or opinion letter regarding a plan's qualification as it is written, not as it operates. Although the letter must be requested from IRS, it is not necessary to obtain such a letter as a condition for the plan to get all of the tax benefits.[141]

If a plan is amended, a determination or opinion letter may be requested to see if the plan continues to qualify with the amendment.

Determination letters are written for individually designed plans. These letters are issued by IRS District offices.

Opinion letters are written for master or prototype plans of sponsoring organizations. These letters are issued by the IRS National Office in Washington.

A master plan has a single trust or custodial account. All employers who adopt a master plan use the single trust or custodial account.

A prototype plan has separate trusts or custodial accounts for each employer who adopts the plan.

Who may request letters? An employer or a plan administrator of an individually designed plan may request a determination letter.

An opinion letter may only be requested by a plan sponsor that is a trade or professional association, a bank, an insurance company, or a mutual fund.

IRS will not issue letters if an employer adopts a master or prototype plan that was previously approved and if the plan's provisions are followed. An opinion letter will not be issued for a defined contribution plan (except a target benefit plan) that tests for discrimination using benefits rather than contributions.

Opinion letters on amendments will not be issued to sponsors of master and prototype plans unless the sponsor assures IRS that within 90 days after a favorable letter is issued, the sponsor will:

1) Give each employer who adopted the plan a chance to decide whether to keep the plan, and if so, to amend it,

2) Advise employers that participation in the plan may not continue without the amendment, and

3) Advise each employer in a prototype plan that the trust agreement may need amending.

How to Request a Letter

Forms are available for requesting opinion and determination letters, depending on the type of plan.

Opinion letter requests should be made on either Form 3672, *Application for Approval of Master or Prototype Defined Contribution Plan for Self-Employed Individuals,* or Form 3672A, *Application for Approval of Master or Prototype Defined Benefit Plan for Self-Employed Individuals.* File these forms with the Internal Revenue Service, Attention: E:EP:T, 1111 Constitution Avenue, N.W., Washington, D.C. 20224.

Determination letter requests should be made on one of the following forms, depending on the type of plan.[142]

Form 5300, *Application for Determination for Defined Benefit Plan,*

Form 5301, *Application for Determination for Defined Contribution Plan, or*

Form 5303, *Application for Determination for Collectively-Bargained Plan.*

Form 5302, *Employee Census,* must also be completed and attached to Forms 5300 and 5301. It may also be required with Form 5303.

These forms should be filed with the IRS District Director for the district where the employer's principal place of business is.

Reporting Requirements

An owner-employee who is the only plan participant in the year and all earlier years is not required to file Form 5500-K, *Annual Return/Report for Employee Pension Benefit Plan for Sole Proprietorships and Partnerships.* Form 5500-K does not have to be filed for partnerships if the only participants are partners who own more than a 10% interest in the partnership.

All other employers with plans or plan administrators must furnish certain information to the Internal Revenue Service annually.

One of the following forms must be filed annually with IRS by the plan administrator or employer.

Form 5500, *Annual Return/Report of Employee Benefit Plan (with 100 or more participants)*

Form 5500-C, *Annual Return/Report of Employee Benefit Plan (with fewer than 100 participants, none of whom is an owner-employee)*

Form 5500-K, *Annual Return/Report of Employee Pension Benefit Plan for Sole Proprietorships and Partnerships (with fewer than 100 participants and at least one owner-employee)*

Additional forms. If they apply, the following forms must be attached to the Form 5500, 5500-C, or 5500-K that is filed.

Schedule A (Form 5500), *Insurance Information,* must be filed if any plan benefits are provided by an insurance company.

Schedule B (Form 5500), *Actuarial Information,* must be filed for most defined benefit plans.

Schedule SSA (Form 5500), *Annual Registration Statement Identifying Separated Participants With Deferred Vested Benefits,* must be filed if during the plan year:

1) A participant separated from the job covered by the plan,

2) The participant is entitled to a deferred vested benefit from the plan, and

3) The participant is not paid retirement benefits from the plan, does not return to the job covered by the plan, and does not forfeit a deferred vested benefit in the plan before the end of

the year after the year the participant left.

If all three conditions are not present for one or more participants who have left, do not file Schedule SSA.

When to file. Form 5500, 5500-C, or 5500-K with required schedules must be filed by the last day of the 7th month after the end of the plan year.

An extension of time up to 2½ months may be granted for filing the forms. Use Form 5558 to request the extension.

If an employer has been granted an extension of time to file the income tax return beyond the due date of Form 5500, 5500-C, or 5500-K, the extension for the income tax return also applies to the return/report for the plan. This applies only for single employer plans in which the plan year and the employer's tax year are the same. A copy of the approved IRS extension for the income tax return must be attached to Form 5500, 5500-C, or 5500-K if filed after the normal due date.

Where to file. Forms should be filed with the Internal Revenue Service Center given in the instructions to the forms.

FOOTNOTES

[1]Section 1.401-10(b)(3)(ii) of the Regulations

[2]Section 1.401-10(b)(3)(i) of the Regulations

[3]Section 1.401-10(b)(1) of the Regulations

[4]Section 1.401-10(b)(2) of the Regulations

[5]Section 1.401-10(c)(2)(iv) of the Regulations

[6]Section 1.401-10(c)(2)(iv) of the Regulations

[7]Section 1.401-10(d) of the Regulations

[8]Section 1.401-10(c)(2) of the Regulations

[9]Rev. Rul. 75-525, 1975-2 C.B. 350

[10]Section 1402(a)(12) of the Code

[11]Section 401(c)(2)(A) of the Code

[12]Section 401(c)(2)(C) of the Code

[13]Rev. Rul. 70-491, 1970-2 C.B. 92

[14]Section 1402(c) of the Code

[15]Section 414(i) and (j) of the Code

[16]Section 414(i) of the Code

[17]Section 1.401-11(b)(3) of the Regulations

[18]Section 414(j) of the Code

[19]Section 1.401-11(d)(1) of the Regulations

[20]Rev. Rul. 71-446, 1971-2 C.B. 187

[21]Section 1.401-11(c)(2)(i) of the Regulations and section 1402 (b) of the Code

[22]Section 1.401-11(c)(2)(ii) of the Regulations

[23]Section 401(j)(4) of the Code

[24]Section 1.401-11(d)(2) of the Regulations

[25]Section 1.401-11(d)(2)(iii)(b) of the Regulations

[26]Section 1.401-11(d)(3) of the Regulations

[27]Section 1.401-11(b)(2) of the Regulations

[28]Rev. Rul. 70-370, 1970-2 C.B. 84

[29]Rev. Rul. 72-302, 1972-1 C.B. 110

[30]Section 1.401 (j)-2(i) of the Proposed Regulations

[31]Rev. Rul. 69-477, 1969-2 C.B. 87

[32]Section 1.401-11(e) of the Regulations

[33]Rev. Ruls. 72-240 and 72-241, 1972-1 C.B. 108

[34]Section 1.72-9 of the Regulations

[35]Section 1.401-11(e)(8) of the Regulations

[36]Section 1.401-13(b)(3) of the Regulations

[37]Section 267(c)(4) of the Code

[38]Section 401(d)(3)(A) of the Code

[39]Section 410(a)(3)(A) of the Code

[40]Section 410(a)(5)(B) of the Code

[41]Section 401(d)(B)(i) of the Code

[42]Section 401(d)(3)(B)(ii) of the Code

[43]Rev. Rul. 68-593, 1968-2 C.B. 182

[44]Rev. Rul. 68-303, 1968-1 C.B. 165

[45]Rev. Rul. 69-66, 1969-1 C.B. 128

[46]Rev. Rul. 65-243, 1965-2 C.B. 139

[47]Section 581 of the Code

[48]Rev. Rul. 68-115, 1968-1 C.B. 166

[49]Section 1.401-12(d)(2) of the Regulations

[50]Rev. Rul. 70-127, 1970-1 C.B. 105

[51]Rev. Rul. 69-524, 1969-2 C.B. 98

[52]Section 1.401-12(h) of the Regulations

[53]Section 1.401-12(i)(1)(ii) of the Regulations

[54]Section 72(m)(7) of the Code

[55]Section 1.401-12(m) of the Regulations

[56]Rev. Rul. 68-160, 1968-1 C.B. 167

[57]Rev. Rul. 73-56 1973-1 C.B. 196

[58]Rev. Rul. 69-254, 1969-1 C.B. 129

[59]Section 72(m)(4) of the Code and section 1.72-17(d)(2) of the Regulations

[60]Section 1.72-17(b)(5) of the Regulations

[61]Rev. Rul. 69-313, 1969-1 C.B. 130

[62]Rev. Rul. 69-380, 1969-2 C.B. 97

[63]Section 404(e)(1) of the Code

[64]Section 404(e)(4) of the Code

[65]Section 404(e)(4) and 415(c)(5) of the Code

[66]Section 404(a)(9)(C) of the Code

[67]Section 404(e)(2)(A) of the Code

[68]Section 404(a)(9)(C) of the Code

[69]Section 1.404(e)-1A(c)(1) & (2) of the Proposed Regulations

[70]Section 1.404(e)-1A(c)(3) of the Proposed Regulations

[71]Section 1.404(e)-1A(c)(4) of the Proposed Regulations

[72]Section 1.401(j)-1(e)(1) of the Proposed Regulations

[73]Section 1.401(j)-1(d) of the Proposed Regulations

[74]Section 1.401(j)-1(e)(2) of the Proposed Regulations

[75]Section 1.401(j)-1(e)(9) of the Proposed Regulations

[76]Section 1.401(j)-1(e)(6) of the Proposed Regulations

[77]Section 1.401(j)-1(e)(7) of the Proposed Regulations

[78]Section 1.401(j)-1(e)(8) of the Proposed Regulations

[79]Section 1.401(j)-1(f)(2) of the Proposed Regulations

[80]Section 1.401(j)-1(f)(3) of the Proposed Regulations

[81]Section 1.401(j)-2(e)(2) of the Proposed Regulations

[82]Section 1.401(j)-1(g)(3)(i) of the Proposed Regulations

[83]Section 1.401(j)-2(f) of the Proposed Regulations

[84]Section 1.401(e)-5(a) of the Regulations

[85]Section 1.401(e)-5(a) of the Regulations

[86]Section 1.401(e)-5(b) of the Regulations

[87]Section 1.401(e)-5(c)(2) of the Regulations

[88]Section 1.401(e)-5(c)(1) of the Regulations

[89]Section 1.404(e)-1A(h) of the Regulations

[90]Section 1.404(e)-1A(g) of the Regulations

[91]Section 4972(b) of the Code

[92]Section 4972(a) of the Code

[93]Section 1.401(e)-4(b)(1)(i) of the Regulations

[94]Section 1.401(e)-4(b)(1)(iv) of the Regulations

[95]Section 415(c)(7) of the Code

[96]Section 401(a)(10)(A)(ii) and (d)(5) of the Code

[97]Section 1.401(e)-4(b)(2)(i) and (ii) of the Regulations

[98]Section 1.401(e)-4(b)(3) of the Regulations

[99]Section 1.401(e)-4(b)(4)(i) of the Regulations

[100]Section 1.401(e)-4(b)(4)(ii) of the Regulations

[101]Section 1.401(e)-4(b)(4)(iii) of the Regulations

[102]Section 1.401(e)-4(b)(5) of the Regulations

[103]Section 401(e) of the Code

[104]Section 404(a)(9) of the Code

[105]Section 404(a)(3) of the Code

[106]Section 404(a)(7) of the Code

[107]Section 412 of the Code

[108]Section 404(a)(6) of the Code

[109]Section 11.404(a)(6)-1(b) and (d) of the Temporary Regulations

[110]Section 11.404(a)(6)-1(c) of the Temporary Regulations

[111]Rev. Rul. 76-28, 1976-1 C.B. 106

[112]Sections 401(f) & (g) of the Code and 1.401-8 & 9 of the Regulations

[113]Section 1.403(a)-1(d) of the Regulations

[114]Rev. Rul. 65-25, 1965-1 C.B. 173

[115]Section 2(a)(15) of the Investment Company Act of 1940

[116]Section 1.401-9 of the Regulations

[117]The Second Liberty Bond Act

[118]Section 405 of the Code and section 1.405-1 of the Regulations

[119]Rev. Proc. 73-6, 1972-1 C.B. 710

[120]Section 1.401-12(c)(5) of the Regulations

[121]Section 401(f) of the Code

[122]Rev. Rul. 66-101, 1966-1 C.B. 86

[123]Section 401(g) of the Code and Rev. Rul. 66-253, 1966-2 C.B. 122

[124]Rev. Rul. 68-533, 1968-2 C.B. 190

[125]Section 72(m)(5) of the Code

[126]Section 72(m)(5)(B) of the Code

[127]Section 1.72-17A(f)(1) & (2) of the Regulations

[128]Section 1.72-17A(f)(4) of the Regulations

[129]Section 1.72-17A(e)(2)(ii)(C) of the Regulations

[130]Section 1.72-17A(e)(2)(i) of the Regulations

[131]Section 1.72-17A(e)(2)(ii) of the Regulations

[132]Section 1.72-17A(e)(2)(iv)(B) of the Regulations

[133]Section 1.72-17A(e)(2)(iv)(C) of the Regulations

[134]Section 1.72-17A(e)(2)(iv)(E) of the Regulations

[135]Section 1.72-17A(d)(1) of the Regulations

[136]Section 1.72-17A(d)(3) of the Regulations

[137]Section 72(d) of the Code

[138]Section 72(a) of the Code

[139]Section 402(e) of the Code

[140]Section 4975 of the Code

[141]Rev. Proc. 72-6, 1972-1 C.B. 710, Rev. Proc. 72-7, 1972-1 C.B. 715, and Rev. Proc. 75-51, 1975-1 C.B. 590

[142]Rev. Proc. 75-47, 1975-2 C.B. 581

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